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Resolving the tension between investor short-termism and long-term sustainability.

How can management respond when shareholders/investors are pressing the company to take actions that may provide short-term financial benefits but may undermine the long-term success of the business?

An Interactive Q&A with the Governance, Risk & Reputation Strategist.

Submitted by Rory Sullivan, independent consultant

Q: "How can management respond when shareholders/investors are pressing the company to take actions that may provide short-term financial benefits but may undermine the long-term success of the business?"

A: The power struggle between short-term financial results and long-term resilience and the creation of a sustainable business model (sometimes at the expense of short-term results) has been raging for some time.

In recent years several developments have heightened this tension. There's the rise of a new and aggressive breed of stakeholders (hedge funds come to mind) that are applying pressure for short-term results because their investment model is based on a quick turn-around.

There is the rise of powerful funds (sovereign and pension funds, for example) that have a longer-term horizon, are more conservative by nature as they represent more conservative investors generally (pensioners, public agencies, and the like) and are generally more focused on good governance and risk management.

Add to this tension the rise of environmental, social and governance (ESG) awareness – i.e. investors, customers, regulators and other stakeholders are more than ever before looking at not only the financial results but also the key non-financial results of companies.

As a result of the ESG movement, there is an "integrated reporting" theme evolving and a number of efforts under way to consolidate and standardize "integrated" financial and ESG reporting, though it is still a work in progress.

Posted by Andrea Bonime-Blanc (on Sep 15, 2014)

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In addition, the prevailing executive pay model continues to overemphasize short-term financial results – which CEOs and their executive teams must accomplish in a short-sighted manner.

And then, of course, you have the rise of technological tools that allow nanosecond investment decisions to be made, with attendant turbulence and potential destabilizing consequences.

Combine all of these elements, stir them up, and the results are a complex and confusing brew that businesses must contend with.

What is the solution?

It's not easy, but it involves aligning leadership (both management and board), culture strategy and risk management. Some great companies – Unilever comes to mind – are already doing this.

Here are some of the key steps companies should focus on to build a long-term strategy:

- Management and the board must be aligned on pursuing the long-term focus
- They have to decide who the most important core stakeholders are (customers, employees, majority of shareholders, others) and develop their long-term strategy around them
- Have a high level and deep understanding of the global risk and reputation profile of the company
- Build an integrated global culture and performance management system that combines financial metrics with sustainability, integrity and risk management objectives
- Having a visionary leader and a responsible and diverse board doesn't hurt

There are a number of studies that have shown the financial value of sustainability to companies. However, the qualitative value of long-termism cannot be forgotten and includes important positives such as stakeholder loyalty and improved reputation.

The more rigor and discipline researchers and practitioners can bring to demonstrating the quantitative and qualitative value of a long-term sustainable approach to business, the more we will be able to demonstrate the value of long-termism. While it is still a work in progress, we're starting to get there.

Long Term Positive Financial Impact of Sustainability[1]			
	An Investment in 1993 of:	Results in 2010 for Sustainable Companies	Results in 2010 for Low/No Sustainability Companies
Investment	$1	$22.6	$15.4
Return on Equity	$1	$31.7	$25.7
Return on Assets	$1	$7.1	$4.4
Source: The Impact of a Corporate Culture of Sustainability on Corporate Behavior and Performance. Robert G Eccles, Ioannis Ioannou and George Serafeim. Working Paper, May 2012.			

1 *Table assembled and reproduced from forthcoming book by Andrea Bonime-Blanc, The Reputation Risk Handbook: A Practical Guide for Managers, Executives and Boards, Dō Sustainability, October 2014.*

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